

# MEASURING FINANCIAL PERFORMANCE THROUGH RATIO ANALYSIS

## “A GENERAL STUDY ON THE RATIO ANALYSIS TOOL TO TRIGGER OUT FINANCIAL PERFORMANCE”

JOY THOMAS<sup>1</sup> & S. RABİYATHULBASARIYA<sup>2</sup>

<sup>1</sup>Research Scholar, Department of Management Studies, Bharath university, Chennai, Tamilnadu, India

<sup>2</sup>Associate Professor, Department of Commerce and Business Administration, Bharath university, Chennai, Tamilnadu, India

### ABSTRACT

*The financial performance execution has a major significance in universe of economy and it was what the investigations of bookkeeping and organization concentrated extraordinarily on. The money related reports which are set up in the organization is considered as a critical instrument to assess the monetary execution where breaking down these reports helps in distinguishing the organization's purposes of shortcoming and quality and work on the shortcoming to discover arrangements. The monetary proportion is the most widely recognized technique used to examine the money related reports and has a precise assessment to treat the purposes of shortcoming, successfully and proficiently. The money related proportions don't include new data yet it is useful in clarifying the connection between the factors to think of results. This finance report on ratio analysis assesses the financial strengths and weakness of company, through Financial Ratio Analysis is to assess the performance of the organization by utilizing proportions as a measuring stick to gauge the effectiveness of the organization. The financial performance provides the detailed information about the firm's financial activities which mirrors the liquidity, movement, productivity and effectiveness of the worry in the field of the back.*

*Proportion investigation has filled in as veritable methods for checking, measuring and enhancing execution in an association. Consequently, the investigation inspects an apparatus for measuring association execution utilizing proportion examination. It likewise finds out the significance of interior and outside monetary reports amid proportion investigation to establish enter connections and results keeping in mind the end goal to assess money related execution. The examination affirmed that there is huge connection between proportion investigation and authoritative exhibitions and in addition budgetary proportions feature the significance of powerful administration of an association. In light of the discoveries of this investigation, it was suggested that budgetary proportions ought to be registered intermittently to uncover territories of qualities and shortcomings, and additionally, proportion examination ought to be utilized to gauge execution as far as the benefit.*

**KEYWORDS:** Ratio Analysis, Liquidity, Profitability, Market, Leverage Ratios & Financial Performance Evaluation

**Received:** Oct 03, 2017; **Accepted:** Oct 24, 2017; **Published:** Nov 20, 2017; **Paper Id.:** IJAFMRDEC20174

### INTRODUCTION

Money related proportions have had a critical impact in assessing the execution and budgetary condition/position of any firm. It characterizes the genuine photo of the firm as for quality or shortcomings and survival position of the firm and aides in estimating the fate of the firm and in this manner empowering the leaders to take diverse operational choices of the firm and take restorative activities for the advancement of the firm.

Proportion investigation doesn't mean simply contrasting diverse numbers or figures from money related articulation like income proclamation, pay explanation, and the accounting report. It's a correlation of current numbers or figures with earlier years, with different organizations, with the business, or even against the economy by and large. Proportions characterize the connections between singular esteems and relate these qualities with past qualities that how an organization had performed before, how is performing on display and may perform later on. There are quantities of monetary proportions utilized as a part of investigation to assess and examine the money related execution and survival position of an organizations or undertakings. In any case, most prominent are, Solvency, Stability, Profitability, Operational proficiency, Credit standing, Structural examination, Effective usage of assets, and Leverage or outer financing.

Money related proportions have had a critical impact in assessing the execution and budgetary condition/position of any firm. It characterizes the genuine photo of the firm as for quality or shortcomings and survival position of the firm and aides in estimating the fate of the firm and in this manner empowering the leaders to take diverse operational choices of the firm and take restorative activities for the advancement of the firm. Proportion investigation doesn't mean simply contrasting diverse numbers or figures from money related articulation like income proclamation, pay explanation, and the accounting report. It's a correlation of current numbers or figures with earlier years, with different organizations, with the business, or even against the economy by and large. Proportions characterize the connections between singular esteems and relate these qualities with past qualities that, how an organization had performed before, how is performing in display and may perform later on. There are quantities of monetary proportions utilized, as a part of investigation to assess and examine the money related execution and survival position of an organizations or undertakings. In any case, most prominent are, Solvency, Stability, Profitability, Operational proficiency, Credit standing, Structural examination, Effective usage of assets, and Leverage or outer financing.

Right off the bat, the cases of bondholders are long haul. They are keen on the income of the firm to benefit obligations over a drawn out stretch of time. The bondholders may assess this by breaking down the capital structures of the firm, the real sources and clients of store, the organizations gainfulness. At last, a financial specialist in an organization s normal stock is concerned chiefly with present and expected future acquiring and also the strength of these winning after some time. Accordingly, the financial specialist, for the most part focuses on breaking down the gainfulness of the firm.

## **STATEMENT OF THE PROBLEM**

Numerous monetary and bookkeeping models were produced amid past decades. In any case, the monetary proportions still kept its established and major power either as a feature of these budgetary and bookkeeping models or as another vital steady examination with it, Because of the demonstrated energy of the proportion investigation in the viable money related and arranging investigation. In spite of the fact that in any case, money related proportions examination has its constraints; which can be abridged as takes after: there is extensive subjectivity required as there is no hypothesis with respect to what ought to be the correct number for the different proportions; proportions may not be precisely similar crosswise over various organizations because of an assortment of components, for example, extraordinary bookkeeping hones and diverse monetary year; proportions depend on budgetary explanations that mirror the past just and are not a sign without bounds; and money related proclamations give an estimation of the expenses and not values. Radiating from the above, to assess firm money related condition and execution, examination and translation of different proportions ought to be given to a gifted examiner. Against this backdrop, the following research questions are used to guide our investigation:

- To what degree does proportion examination make effect on firm execution assessment?
- To what degree does use proportion influence firm execution assessment?
- To what degree does showcase proportion influence firm execution assessment?
- To what degree does benefit proportion influence firm execution assessment?

## **OBJECTIVES OF THE STUDY**

- To assess the effect of proportion investigation on firm money related execution.
- To research the impact of proportions on firm execution assessment.
- To decide the points of interest and restriction of proportion examination on firm execution assessment.

## **LITERATURE REVIEW**

Execution assessment of an organization is generally identified with how well an organization can utilize its resources, investor value and risk, income and costs. Money related proportion investigation is extraordinary compared to other devices of execution assessment of any organization. With a specific end goal to decide the money related position of the organization and to make a judgment of how well an organization is proficient in its operation and administration and how well the organization has possessed the capacity to use its benefits and gain benefit distinctive strategies and additionally apparatuses are utilized, among which is the monetary proportions. Money related proportion can be viewed as a connection between a two individual quantitative budgetary data associated with each other in some intelligent way, and this association, is considered as a significant monetary pointer which can be utilized by the distinctive monetary data clients.

Brigham and Ehrhardt (2016) express that, money related proportions are intended to help assess budgetary proclamations. Budgetary proportions are utilized as an arranging and control instrument. Budgetary proportions are utilized by inner and outer money related information clients, in settling on their financial choices; including contributing, and execution assessment choices. Money related proportions investigation is utilized to assess the execution of an association so as to decide the solid and frail focuses and it offers arrangements by giving suitable plans. In any case, an extensive number of norms and different money related proportions exist yet the selection of proportions utilized relies upon the movement of the association and the reason for examination.

James (2014), Pronounce that it is the investigation of budgetary proclamations that is utilized to quantify organization execution. On the off chance that the proportions show poor execution, financial specialists might be hesitant to contribute. Accordingly, the present working capital proportion measures current resources against current liabilities. The present proportion measures the organization's capacity to pay back its fleeting obligation commitments with its present resources. Wherefore, the analysis proportion or snappy proportion, measures fast resources against current liabilities. Snappy resources are considered resources that can be immediately changed over into money. By and large they are present resources less stock. The present proportion is computed by isolating current resources by current liabilities. Current resource incorporates stock, exchange indebted individuals, advances, stores and reimbursement, interest in attractive securities in here and now advance, money and money reciprocals, and current liabilities are contained here and now banks advance, long haul advances current bit, exchange lenders liabilities for other back and so on. Use Ratio and

Firm Performance Evaluation Leverage proportion indicates how proficient the association utilizes other individual's cash and whether, it is utilizing a considerable measure of acquired cash (Lasher, 2015).

Abu Hasheesh (2013), analyzed the part of distributed bookkeeping Information in foreseeing share costs. The investigation utilized a specimen of 40 open organizations recorded in Amman Security Exchange for the year. The outcomes demonstrated that there is a positive noteworthy positive connection between the market cost per share with the proportions of net benefits to value, net benefits to adding up to resources, and profits to net benefits as an aggregate. The outcomes indicated additionally a huge negative connection between the market costs per share; with the proportions of settled advantages for add up to resources, the lenders aggregate to aggregate of money sources, and the wages proportion to aggregate of costs proportion.

Thachappilly (2009), likewise express that the Liquidity Ratios help Good Financial. He knows that a business has high productivity, it can confront here and now monetary issues and its assets are secured up inventories and receivables not feasible for quite a long time. Any inability to meet these can harm its notoriety and financial soundness and in outrageous cases even prompt chapter 11. Also, liquidity proportions are work with money and close money resources of a business on one side, and the prompt installment commitments (current liabilities) on the opposite side. The close money resources for the most part incorporate receivables from clients and inventories of completed products and crude materials. Combined with, current proportion works with every one of the things that go into a business' working capital, and give a snappy take a gander at its transient money related position. Current resources incorporate Cash, Cash reciprocals, Marketable securities, Receivables and Inventories. Current liabilities incorporate- Payables, Notes payable, accumulated costs and impose, and accrued portions of term obligation).  $\text{Current Ratio} = \text{Current Assets} / \text{Current Liabilities}$ . Correspondingly, Quick proportion bars the illiquid things from current resources and gives a superior perspective of the business' capacity to meet its developing liabilities.  $\text{Speedy Ratio} = \text{Current Assets less (Inventories + Prepaid costs + Deferred wage charges + other fluid things)} / \text{Current Liabilities}$ . In the last proportion under this article is money proportion. Money proportion rejects even receivables that can set aside a long opportunity to be changed over into money.  $\text{Money Ratio} = (\text{Cash} + \text{Cash counterparts} + \text{Marketable Securities}) / \text{Current Liabilities}$ .

### **Financial Performance - the Evaluation**

In today's economic world, the financial evaluation performance plays an important role in the administration of accounting. The reports of financial evaluation which is been prepared by the company by itself is considered very vital tool to analyze the financial performance, which helps in finding the strength and weakness as to find the proper solution. The very major method used to analyze the financial reports is the financial ratio which tells the accuracy evaluation of weakness effectively and efficiently. It does not add any new information but it tells the relationship between the variables to give the better results.

### **Advantages of Ratio Analysis**

The slant in costs, deals, benefits and different actualities can be known by processing proportions of pertinent bookkeeping figures of most recent couple of years. This pattern examination with the assistance of proportions might be valuable for estimating and arranging future business exercises.

- Budget is a gauge of future exercises on the premise of past understanding. Bookkeeping proportions help to assess planned figures. For instance, deals spending plan might be set up with the assistance of investigation of

past deals.

- Ratio examination demonstrates the level of proficiency in the administration and use of its advantages. Diverse movement proportions demonstrate the operational effectiveness. Truth be told, dissolvability of a firm relies on the business incomes produced by using its benefits.
- Ratios are compelling methods for correspondence and assume a fundamental part in educating the position of and advance made by the business worry to the proprietors or different gatherings.
- Ratios may likewise be utilized for control of exhibitions of the diverse divisions or branches of an endeavor and additionally control of expenses.
- Comparison of execution of at least two firms uncovers effective and wasteful firms, consequently empowering the wasteful firms to receive reasonable measures for enhancing their proficiency. An ideal method for between firm correlations is to think about the pertinent proportions of the Organization with the normal proportions of the business.
- Ratio examination surveys the liquidity position i.e., here and now obligation paying capacity of a firm. Liquidity proportions demonstrate the capacity of the firm to pay and help in credit examination by banks, lenders and different providers of here and now advances.

#### **Impediments to Ratio Analysis**

- Ratios are computed from the data recorded in the money related explanations. Be that as it may, monetary proclamations experience the ill effects of various confinements and may, thusly, influence the nature of proportion investigation.
- Financial proclamations give authentic data. They don't reflect current conditions. Subsequently, it isn't helpful in anticipating what's to come.
- Different bookkeeping strategies in regards to valuation of inventories, charging devaluation and so forth make the bookkeeping information and bookkeeping proportions of two firms non-practically identical.
- No settled gauges can be set down for perfect proportions. For instance, current proportion is said to be perfect if current resources are double the present liabilities. Be that as it may, this conclusion may not be reasonable if there should be an occurrence of those worries which have satisfactory courses of action with their financiers for giving assets when they require, it might be superbly perfect if current resources are equivalent to or marginally more than current liabilities.
- Proper mind must be taken when translating bookkeeping proportions ascertained for occasional business. For instance, an umbrella organization maintains high stock amid stormy season and for whatever remains of year its stock level ends up noticeably 25% of the regular stock level. Thus, liquidity proportions and stock turnover proportion will give one-sided picture.

#### **FINDINGS AND RECOMMENDATIONS**

This research work studied how ratio analysis can be used to measure the performance of an organization. Based on the discussions and findings in the course of this study, the following conclusions are made:

- Ratio analysis is a tool of financial analysis, which can be used as a predictive tool for measuring business performance.
- Ratio analysis can be used to show areas of strengths and weaknesses of a company.
- Ratio analysis is required for management control decisions, investment decisions and credit control purposes.
- Ratio analysis is required to determine whether a company have been improving or is deteriorating financially over a period of time.
- Ratio analysis can be used to determine whether a company have met the required standard within the industry.
- Profitability ratios are useful to the management of a company. They are used to determine the profitability of a company and the efficiency in the utilization of the resources of a company.

Therefore, the following recommendations are made

- Ratio analysis should form part of management activities and should be computed periodically to reveal areas of strengths and weaknesses of a company.
- Ratios should be used by the management to measure the profitability of the company and to compare the financial activities of the company with that of other companies within the same industry. This helps to determine whether the company has performed up to the standard required by the industry.
- The investors should use investment ratios to determine how much dividend will accrue to them.
- Creditors and loan providers are advised to check the liquidity of a company before granting loans or giving any consideration. Therefore, they should consider ratios such as current ratio and quick assets ratio.
- The employees of an organization should be interested in ratios such as the long-term solvency and liquidity ratios. This enables the employees to know and measure the security of their jobs.

## CONCLUSIONS

Ratio analysis has served as a veritable means of monitoring, measuring and improving performance in an organization. Hence, the study examines a tool for measuring organization performance using ratio analysis. It also ascertains the relevance of internal and external financial reports during ratio analysis for the purpose of establishing key relationships and results in order to appraise financial performance.

## REFERENCES

1. Abu Hasheesh (2013), "Accounts Receivable: Analyzing the Turnover Ratio", *Journal of account receivable*.
2. Brigham and Ehrhardt (2016), "Intermediate accounting: cash ratio analysis". (10<sup>th</sup> ed). Bearcat Company, Vol-1, p.211.
3. Hutchinson, James (2016), "Long Term Debt to Equity Ratio of a Business: Understand a Company's Value to its Investors and Owners", *Journal of long term debt to equity ratio*.
4. *Indian Journal of finance* -Dr Ashok Khurana – November 2009.
5. James (2014), "Contribution Margin and Breakeven Analysis: Determining when a Company will Realize a Profit", *Journal of contribution margin and breakeven analysis*.

6. Lasher 2015, *Financial Services and Financial Institutions: Value Creation in Theory and Practice* Prentice Hall.
7. Thachappilly, Gopinathan. (2009). “Profitability Ratios Measure Margins and Returns: Profit Ratios Work with Gross, Operating, Pretax and Net Profits”. *Journal of profitability ratio measure margin and return*.
8. Zain, Maria. (2008). “How to Use Profitability Ratios: Different Types of Calculations that Determine a Firm's Profits ””, *Journal of profitability ratio analysis*.

